

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of }
ROSE SPAIN }

For Appellant: Richard P. Bateen, Attorney at Law

For Respondent: Burl D. Lack, Chief Counsel;
Israel Rogers, Assistant Counsel

O P I N I O N

This appeal is made pursuant to Section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Rose Spain against proposed assessments of additional personal income tax in the amounts of \$701.03, \$1,979.90 and \$1,424.51 for the years 1953, 1954 and 1955, respectively.

James E. Spain died on September 13, 1949; final distribution of his estate did not occur until December 20, 1957. The Franchise Tax Board contends that the administration of Mr. Spain's estate was unreasonably prolonged and that for tax purposes the estate must be deemed to have been concluded by December 31, 1952.

Appellant and her husband, James E. Spain, engaged in a partnership, known as "J. E. Spain Shoe Departments," which operated shoe departments in space leased from stores located in San Diego, San Bernardino and Pasadena. In 1945 Appellant and her husband transferred their interest in the Pasadena shoe business, in trust, to their two then minor sons. Mr. Spain participated in the management of the Pasadena shoe business until the time of his death in 1949.

The decedent's will named Appellant as executrix and provided that after the fulfillment of certain specific bequests not material here, the residue of the estate was to be transferred to a testamentary trust to be administered by Appellant and her two sons as cotrustees. Appellant was to receive the income on the trust for life and upon her death the trust corpus was to be distributed to the two sons,

Prior to his death, the Internal Revenue Service asserted income tax deficiencies against Mr. Spain for the years 1946 and 1947, on the ground that a portion of the income of the

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Pasadena business held in trust for his sons was taxable to him due to his participation in the operation. On March 10, 1950, these deficiencies, in the total amount of \$41,216.05, including interest, were assessed against decedent. They were paid by the estate the following month and claims for refund were filed. In the latter part of 1951, a settlement of the claims was negotiated and stipulated to in a tax court case allocating a reduced percentage of the disputed income for 1946 and 1947 to decedent.

In July of 1952 the Federal authorities assessed tax deficiencies against decedent in the total amount of \$16,182.12 for the years 1948 and 1949, on the same ground upon which the earlier assessments were made. The latter assessments used the same percentage of income settled upon in the earlier claims. The estate paid the assessments in August of 1952 and claims for refund were filed on June 15, 1954. These claims were compromised by conference at the revenue agent level in December of 1956 based upon a substantial decrease in the percentage of income allocated to decedent. The decrease in the percentage used was due to a decline in Mr. Spain's health which justified attributing less income to his personal services in 1948 and 1949. A final income tax refund, in the amount of \$5,114.21, was received in March of 1957 and closing of the estate was completed in December of that year.

On the ground that the administration of Mr. Spain's estate should have been terminated by December 31, 1952, Respondent added the income of the estate for later years to the income of the Appellant, who was the life income beneficiary of decedent's testamentary trust.

Section 17731, subdivision (a)(3) of the Revenue and Taxation Code provides that income received by an estate of a deceased person during the period of administration or settlement of the estate is taxable to the estate. Respondent's regulations provide:

The period of administration or settlement is the period actually required by the administrator or executor to perform the ordinary duties of administration, such as the collection of assets and the payment of debts, taxes, legacies, and bequests, whether the period required is longer or shorter than the period specified under the applicable local law for settlement of the estates.... However, the period of administration of an estate cannot be unduly prolonged. If the administration of an estate is unreasonably prolonged, the estate is considered terminated for income tax purposes after the expiration of a reasonable period for the performance by the executor of all the duties of administration. (Cal. Admin. Code, Tit. 18, Reg. 17731(g).)

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Section 17731 is similar to Section 641(a)(3) of the 1954 Internal Revenue Code, and the quoted regulation is substantially the same as the Federal Tax Regulations Section 1,641(b)-3.

The question presented is whether the administration of Mr. Spain's estate was unduly prolonged and extended beyond the period required by the executor to perform his ordinary duties. We fail to see why the settlement of the estate's tax obligations should not be considered to be included in the executor's "ordinary duties." Indeed, Respondent's own regulation mentions the payment of taxes as being included in such duties.

The Franchise Tax Board does not contend that the estate's prosecution of its claims for refund of Federal income tax were not bona fide or ~~that~~ the time required to settle them was excessive. It is undisputed that the estate pursued settlement in a reasonably diligent manner. Respondent merely argues that the negotiations for refund could just as easily have been handled by the trustees of decedent's testamentary trust as by the executrix. Respondent's argument misses the issue. Assuming that the refund negotiations could have been carried on as easily by the trustees as by the executrix, we are of the opinion that the plain meaning of Respondent's regulations prohibit it from asserting that an estate was unduly prolonged where the executor has merely performed his ordinary duties and the performance of those duties has not been unduly delayed.

Our conclusion is supported by Federal authorities which have recognized that the settlement of disputed claims, including litigated tax disputes, is a valid reason for the continued administration of an estate. (Estate of Robert W. Harwood, 46 B.T.A. 750; Edwin M. Petersen, 35 T.C. 962, 973; A. T. Miller, 39 T.C. 940.) For the purpose at hand, we see no significant difference between litigating a tax claim in court and pursuing it before the administrative agency which assessed the tax.

Respondent relies upon Estate of J. F. Hargis, 19 T.C. 842, for the proposition that the negotiation of tax refunds does not constitute a valid reason for keeping the estate open. In addition to the fact that the court did not make a specific holding to this effect, we think the case is clearly distinguishable in that the main probate proceeding was terminated in the year the Tax Court found that the estate should have closed. In that year a final accounting was filed and the state probate court found that there was no necessity for continued administration, approved the final account, closed the estate, discharged the administrator and released his bondsmen. The Tax Court found that although an ancillary proceeding in another state, involving a very small proportion of the entire assets, was not closed until the following year, all the normal duties pertaining to the administration of the estate had been carried out. The formal

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closing of the main probate proceeding, which influenced the court, is a factor which is not present in the instant appeal.

O R D E R

Pursuant to the views expressed in the opinion of the Board on file in this proceeding; and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to Section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Rose Spain against proposed assessments of additional personal income tax in the amounts of \$701.03, \$1,979.90 and \$1,424.51 for the years 1953, 1954 and 1955, respectively, be and the same is hereby reversed.

Done at Sacramento, California, this 1st day of October, 1963, by the State Board of Equalization.

John W. Lynch, Chairman

Geo. R. Reilly, Member

Paul R. Leake, Member

Richard Nevins, Member

 , Member

ATTEST: H. F. Freeman, Executive Secretary